

Relationship Between Personal Income and Adjusted Gross Income, 1947-78

THIS article presents a reconciliation of the Bureau of Economic Analysis (BEA) measure of personal income with the Internal Revenue Service (IRS) measure of adjusted gross income for 1947-78 and introduces important new information: an allocation of the residual difference, or gap, between the BEA and IRS income measures among the various types of income.¹

Description of the income series

Personal income is the income received by persons from all sources, that is, from participation in production, from transfer payments from government and business, and from government interest, which is treated like a transfer payment. Persons consist of individuals, nonprofit institutions, private noninsured welfare funds, and private trust funds. Proprietors' income is treated in its entirety as received by individuals. Life insurance carriers and private noninsured pension funds are not counted as persons, but their saving is credited to persons. Personal income is the sum of wage and salary disbursements, other labor income, proprietors' income with inventory valuation and capital consumption adjustments, rental income of persons with capital consumption adjustment, personal dividend income, personal interest income, and transfer payments, less personal contributions for social insurance.

Adjusted gross income (AGI) is the

total income from all sources that is subject to individual income tax less certain deductions. The total income subject to tax includes wages and salaries, a portion of dividends, interest, and pension income, net business and farm income, net capital gains income, and other miscellaneous items. Deductions allowed in the calculation of AGI include various expenses considered necessary in earning income, cap-

tain allowances for capital gains and losses, contributions to retirement funds by the self-employed, and a portion of sick pay.

Personal income not included in AGI

Personal income and AGI each include items that the other omits by definition. Line 2 of table 1 is the sum of seven groups of items (lines 3-9) that are included in personal income but not in AGI because they are not taxable under the individual income tax. The largest (line 3) consists of all government and business transfer payments except taxable retirement benefits paid to former government employees. The second largest (line 4) consists of other labor income except fees; the major components of other labor income are pension and profit sharing, group insurance, workmen's compensation, and supplemental unemployment benefits. (See NIPA table 6.15 for detail.) The third largest (line 5) consists of all imputed income included in personal income. No deduction is made for an unknown amount

Table 1.—Reconciliation of Personal Income and Adjusted Gross Income, 1977-78

(Billions of dollars)			
	Line	1977	1978
Personal income.....	1	1,538,017	1,728,748
Less: Portion of personal income not included in adjusted gross income, total.....	2	394,460	487,488
Transfer payments except taxable military retirement and taxable government pensions.....	3	180,281	199,040
Other labor income except fees.....	4	87,862	100,828
Imputed income in personal income.....	5	48,077	50,429
Investment income retained by life insurance carriers and noninsured pension funds.....	6	20,268	30,067
Investment income received by nonprofit institutions or retained by fiduciaries.....	7	11,523	13,020
Differences in accounting treatment between NIPA's and tax regulations, net.....	8	11,807	13,596
Other personal income exempt or excluded from adjusted gross income.....	9	28,193	31,483
Plus: Portion of adjusted gross income not included in personal income, total.....	10	107,227	131,682
Personal contributions for social insurance.....	11	61,106	66,644
Net gain from sale of assets.....	12	31,261	34,488
Taxable private pensions, small business corporation income.....	13	18,919	21,014
Other income in adjusted gross income but not in personal income.....	14	1,979	2,536
Equals: BEA-derived adjusted gross income.....	15	2,874	3,651
Less: Difference between BEA and IRS measures of adjusted gross income (AGI gap).....	16	1,250,688	1,406,865
Equals: Adjusted gross income of IRS.....	17	82,186	108,619
Equals: Adjusted gross income of IRS.....	18	1,188,492	1,382,447

2. The 1978 net differences in accounting procedures between the NIPA's and tax regulations (line 8, table 1) consists of the following (millions of dollars):

Capital consumption adjustment.....	-9,928
Excess of tax depreciation over the NIPA measure of depreciation for farm proprietors' income and for rental income of persons.....	16,068
Inventory valuation adjustment for nonfarm, noncorporate business.....	-2,150
Change in farm inventories.....	-60
Gains arising from sale of livestock, timber, and certain real estate.....	2,545
Excess of the interest accrued over the interest paid on U.S. savings bonds.....	2,297
Depletion and certain deductible oil, gas, or geothermal well drilling expenses.....	2,534
Bad debt.....	1,369
Total.....	12,508

1. Table 8.18 of the volumes that present the results of the 1980 comprehensive revision of the national income and product accounts (NIPA's) shows a reconciliation for 1947-78. See the *National Income and Products Accounts of the United States, 1939-76: Statistical Tables* and the *National Income and Product Accounts, 1970-79*. The estimates for 1977 and 1978 have been revised on the basis of new IRS data.

of imputed income, believed small, that is actually included in AGI. (NIPA table 8.8 provides details of imputed income.) Additional major categories are investment income retained by life insurance carriers and noninsured pension funds (line 6) and received by non-profit institutions or retained by fiduciaries (line 7).

Differences in accounting procedures introduce a difference between personal income and AGI that is shown on a net basis in line 8. The differences in accounting procedures result largely from the introduction in the NIPA's of procedures designed to value capital consumption and inventory change of all firms at current prices, and to apply accounting conventions that are uniform for all firms and at all time periods.⁵

The capital consumption adjustment subtracted in BEA-derived AGI is the sum of the capital consumption adjustment for farm and nonfarm proprietors' income and for rental income of

persons, excluding the amount for owner-occupied dwellings.⁶ In the NIPA's, capital consumption allowances are based on consistent accounting and valued in current prices, while the IRS depreciation is based on varying service lives and depreciation formulas, and is valued in historical costs. Tax return data are not the starting point for the NIPA measure of depreciation associated with farm proprietors' income and rental income of persons, and the published capital consumption adjustment relates only to the adjustment for current replacement cost. Therefore, for these types of income the adjustment for consistent accounting at historical cost is the excess of tax depreciation over the NIPA depreciation.

The inventory valuation adjustment for nonfarm, noncorporate business is the difference between the book value

8. In the NIPA's, capital consumption allowances consist of depreciation and accidental damage to fixed capital.

and current-price value of inventories used up in production. Personal income excludes this difference but AGI includes it.

The difference in the estimates of change in farm inventories in the NIPA's and AGI is also subtracted from personal income. Change in farm inventories in the NIPA's is based on the U.S. Department of Agriculture estimates of change in the physical quantities of inventories of harvested crops and of livestock owned by farmers valued at market price. Change in farm inventories in AGI is based on the amount of inventory reported in the cost of goods sold on Schedule C, Form 1040. Farmers are required to use inventories in computing gross income from their businesses only if they elect to use the accrual method of accounting for their profit or loss from the sale of farm products.

Gains arising from sale of livestock, timber, and certain real estate are ac-

Table 2.—Reconciliation of Personal Income and Adjusted Gross Income, by Type of Income, 1978

(Billions of dollars)

	Personal Income									Income not included in personal income
	Total	Wages and salaries	Proprietors' income ¹		Personal dividend income	Rental income of persons ²	Personal interest income	Taxable pensions	Other personal income	
			Farm	Nonfarm						
Personal income.....	1,721.8	1,305.2	26.1	98.9	42.1	27.4	171.2	24.2 ⁴	231.6 ⁴	0
Less: Portion of personal income not included in adjusted gross income, total.....	437.5	0.2	7.6	4.3	7.3	14.3	72.7	0	290.0	23.4 ⁴
Transfer payments except taxable military retirement and taxable government pensions.....	100.0	0	0	0	0	0	0	0	100.0	0
Other labor income except fees.....	100.8	0	0	0	0	0	0	0	100.8	0
Imputed income in personal income.....	50.4	3.0	3.2	7.7	0	3.8	30.7	0	0	0
Investment income retained by life insurance carriers and noninsured pension funds.....	30.1	0	0	0	0	0	30.1	0	0	0
Investment income received by nonprofit institutions or retained by fiduciaries.....	13.0	0	-	.5	5.7	.0	6.2	0	0	0
Differences in accounting treatment between NIPA's and tax regulations, net.....	12.0	0	4.3	3.1	0	8.0	2.3	0	0	0
Other personal income exempt or excluded from adjusted gross income.....	31.8	4.3	0	0	1.5	0	3.3	0	0	22.4 ⁴
Plus: Portion of adjusted gross income not included in personal income, total.....	231.7	0	0	.1	0	.0	0	21.0	89.6	23.4 ⁴
Personal contributions for social insurance.....	68.6	0	0	0	0	0	0	0	68.6	0
Net gain from sale of assets.....	24.5	0	0	0	0	0	0	0	0	24.5
Taxable private pensions.....	31.8	0	0	0	0	0	0	21.8	0	0
Other types of income.....	5.9	0	0	.1	0	.9	0	0	0	4.9
Intercompany reallocation.....	0	1.4	0	1.6	0	0	-1.5	0	-1.4	0
Equals: BEA-derived adjusted gross income.....	1,465.6	1,297.3	18.4	88.4	38.6	14.0	89.0	45.0	0	7.8
Adjusted gross income of IRS (reallocated).....	1,382.4	1,092.8	4.7	67.8	38.2	6.1	62.8	32.7	0	7.9
Adjusted gross income gap.....	103.5	7.0	13.8	20.5	6.8	7.8	25.5	12.1	0	0
Percent distribution of adjusted gross income gap.....	100.0	6.8	13.3	19.8	6.6	7.6	24.3	12.7		
AGI gap as a percentage of BEA-derived AGI.....	7.4	.6	74.6	23.3	18.1	60.0	35.9	28.9		
AGI-IRS as a percentage of BEA-derived AGI.....	92.6	99.4	35.4	78.7	83.9	44.0	64.2	71.4		

¹ Less than \$.1 billion.

² With inventory valuation and capital consumption adjustments.

³ With capital consumption adjustment.

⁴ Consists of the taxable portion of government transfer payments to persons included in personal income. They are government employee retirement benefits in excess of employees' contributions and nondisability military retirement pay.

⁵ Consists of other labor income, nontaxable portion of government transfer payments to persons, business transfer payments, less personal contributions for social insurance.

⁶ Statutory adjustments.

⁷ Net gain from sale of assets, which is the sum of sales of capital assets (net gain less loss) and sales of property other than capital assets (net gain less loss), Small Business Corporation net profit less loss, and all other sources (net).

Table 3.—BEA-derived Adjusted Gross Income by Type of Income, 1947-78

(Billions of dollars)								
Year	Total	Wages and salaries	Pensions and annuities	Farm proprietors' income	Nonfarm proprietors' income	Personal dividend income	Rental income of persons	Personal interest income
1947	172.7	118.5	0.6	14.3	21.7	6.7	6.0	3.8
1948	183.7	131.9	0.7	13.1	22.6	6.4	6.6	4.1
1949	184.0	131.8	0.7	11.2	21.8	6.7	6.6	4.6
1950	202.7	145.1	0.7	10.3	24.2	6.1	6.9	5.1
1951	229.2	167.7	0.8	11.9	28.8	7.8	6.3	5.6
1952	241.0	181.1	1.0	11.1	28.1	7.8	6.6	5.8
1953	258.7	194.6	1.2	10.7	27.0	7.8	6.7	6.0
1954	254.9	192.5	1.3	8.9	28.0	7.6	6.6	7.2
1955	275.0	203.8	1.6	7.9	29.6	8.8	6.3	7.9
1956	285.5	225.6	1.8	7.5	30.7	6.4	6.4	8.9
1957	306.1	238.6	2.1	7.4	32.0	6.6	6.6	10.3
1958	312.8	237.9	2.4	9.0	32.9	9.5	6.7	11.1
1959	334.2	256.4	2.8	7.6	34.2	10.2	6.9	12.3
1960	345.1	268.2	3.2	8.3	32.7	10.6	6.4	12.4
1961	368.4	276.7	3.6	8.4	34.8	11.2	6.3	14.1
1962	380.7	294.1	4.2	8.2	34.9	12.0	6.1	15.0
1963	400.8	309.4	4.7	7.9	35.6	12.8	6.5	17.9
1964	434.0	332.1	5.5	8.0	38.5	14.1	6.9	20.1
1965	457.8	357.4	6.3	8.6	40.9	15.8	7.2	22.8
1966	512.0	392.7	7.4	10.8	43.4	16.6	7.0	25.6
1967	548.3	420.6	8.5	7.0	45.4	16.3	7.1	27.8
1968	599.9	462.6	9.4	8.7	48.4	17.7	7.6	30.7
1969	652.7	508.7	11.0	10.3	49.7	18.0	7.7	35.4
1970	696.1	542.1	12.9	9.0	49.6	17.7	7.4	40.7
1971	730.5	578.1	15.3	9.2	52.0	18.2	8.3	43.6
1972	808.3	628.8	17.9	13.4	58.6	18.5	9.9	46.4
1973	901.4	697.7	20.8	23.1	59.7	21.6	11.1	55.3
1974	978.6	760.3	24.4	21.6	62.0	23.9	12.2	66.3
1975	1,010.6	800.6	28.8	14.4	64.3	24.8	11.2	70.1
1976	1,132.1	833.8	38.0	14.6	73.8	26.6	11.3	78.4
1977	1,250.7	977.0	40.1	10.5	82.0	32.1	13.4	87.7
1978	1,406.0	1,087.3	45.8	18.5	88.4	36.0	14.0	99.9

1. With inventory valuation and capital consumption adjustments.
2. With capital consumption adjustment.

Table 4.—Adjusted Gross Income of IRS by Type of Income, 1947-78

(Billions of dollars)								
Year	Total	Wages and salaries	Pensions and annuities	Farm proprietors' income	Nonfarm proprietors' income	Personal dividend income	Rental income of persons	Personal interest income
1947	168.7	115.3	0.2	3.7	19.7	4.8	2.5	1.9
1948	183.5	130.4	0.3	4.0	20.7	5.0	2.6	2.2
1949	180.6	125.4	0.4	3.4	18.4	5.2	3.1	2.5
1950	178.1	120.6	0.4	3.7	18.9	6.2	3.3	2.7
1951	202.3	151.1	0.5	4.0	21.1	6.1	3.4	2.8
1952	215.3	171.1	0.6	4.9	21.0	6.8	3.5	2.9
1953	228.7	188.3	0.7	4.0	21.3	6.9	3.6	2.9
1954	220.2	187.1	0.8	3.8	21.9	7.8	3.3	2.7
1955	248.5	202.1	0.9	3.8	23.8	7.9	3.5	2.9
1956	267.7	217.2	1.0	4.1	26.1	8.4	3.5	3.2
1957	290.3	229.3	1.1	3.9	26.0	8.1	3.4	3.6
1958	281.2	229.4	1.3	4.3	28.7	8.7	3.4	4.0
1959	335.1	280.8	1.5	3.2	27.9	9.4	3.4	4.7
1960	310.3	260.1	1.6	3.3	28.9	9.6	3.5	5.4
1961	329.0	260.1	1.9	3.0	27.8	10.0	3.4	6.5
1962	348.7	281.0	2.2	4.0	29.4	10.6	3.8	7.5
1963	368.8	302.8	2.7	3.3	30.0	11.6	3.5	8.6
1964	394.7	323.5	3.1	3.2	32.3	11.9	3.4	10.5
1965	428.2	390.4	3.6	4.0	34.7	13.0	3.5	11.7
1966	468.5	381.1	4.4	4.0	28.8	14.0	3.5	12.8
1967	504.8	411.6	5.9	3.0	26.8	14.2	3.5	13.5
1968	554.4	451.5	6.0	3.6	43.0	15.2	3.7	17.5
1969	603.5	493.8	6.9	4.2	41.6	15.7	3.5	20.8
1970	631.7	521.8	7.9	2.4	41.0	16.5	3.5	23.0
1971	673.6	563.0	9.3	2.7	42.6	15.7	3.8	25.7
1972	745.0	622.4	11.0	4.8	45.0	16.8	4.5	28.8
1973	827.1	697.2	13.2	5.7	48.1	18.7	5.4	32.5
1974	905.3	758.8	16.7	8.3	49.1	20.0	5.8	41.2
1975	947.8	795.5	20.9	4.7	49.4	21.9	5.7	45.2
1976	1,033.9	891.6	24.8	4.5	55.6	24.5	6.3	50.6
1977	1,158.5	989.4	28.2	1.1	62.6	27.0	5.7	56.6
1978	1,302.4	1,080.3	32.7	4.7	67.8	30.2	6.1	63.5

Note.—The IRS figures shown in the table for wages and salaries, farm proprietors' income, nonfarm proprietors' income, rental income of persons, and personal interest income reflect reallocations from those shown in *Statistics of Income, Individual Income Tax Returns*. (1) Deductible business expenses and sick pay prior to 1964 and small amount of wages reported on Form 1040A prior to 1969 are added to wages and salaries. The pre-1964 income tax return forms had no specific line for deductible business expenses. Taxpayers were instructed to deduct employee business expenses from wages and salaries before making the entry on the tax return. Similarly, the pre-1964 tax forms had provided a line for the subtraction of excludable sick pay from wages and salaries, and the net amount was tabulated as wages and salaries. The 1964 tax form provided, for the first time, for the entry of gross wages and salaries and for separate lines for statutory adjustments. Prior to 1966, a small amount of income, primarily wages not exceeding \$300 per return (\$200 per return for tax years 1958-65) reported on Form 1040A, for which no tax was withheld, was tabulated not as wages and salaries but as other sources of income in *Statistics of Income*. (2) Income of partnerships is allocated between farm and nonfarm sources using information contained in *Statistics of Income, Business Income Tax Returns*. (3) Income reported under the estate and trust heading on the individual income tax returns is allocated to farm proprietors' income, nonfarm proprietors' income, rental income of persons, and personal interest income using information contained in *Statistics of Income, Fiduciary Income Tax Returns*. The reallocation of partnership income and estate and trust income was undertaken to bring the IRS classification of AGI more in line with the BEA income classification.

recorded a tax treatment similar to a long-term capital asset in AGI, but they are treated as an ordinary income in the NIPA's. All capital gains are excluded from personal income but included in AGI. Thus, capital gains as reported in *Statistics of Income* are added to personal income (line 12) in the reconciliation. But the IRS figures for realized capital gains (net gain less loss) include gains arising from sale of livestock, timber, and certain real estate. Consequently, the latter is subtracted from personal income to prevent double counting. Interest on U.S. savings bonds is recorded on an accrual basis in personal income, but is mostly reported on a cash basis in AGI. Thus, the excess of interest accrued over interest paid is subtracted from personal income. Other accounting differences are in the treatment of depletion, certain oil and gas drilling expenditures, and bad debt.

Line 9 shows the sum of other types of income exempt or excluded from AGI, such as sick pay, interest on State and local government bonds, moving expenses, and alimony payments.

AGI not included in personal income

Line 10 of table 1 is the sum of five groups of items (lines 11 through 15) that are included in AGI but not in personal income. The largest, personal contributions for social insurance (line 11), consists of payments by employees, the self-employed, and other individuals who participate in government social insurance programs. (NIPA table 8.6 provides details.) Net gain from sale of assets (line 12) consists of gains derived from the sale of investment property, such as stocks, bonds, real estate, and from the sale of property other than capital assets. Payments of taxable private pensions (line 13) are not included in personal income. Other types of income in AGI but not in personal income are net income of qualified small business corporations who choose to be taxed as partners (line 14) and a number of small items grouped in line 15. The latter includes noncorporate special assessments, alimony received, and such miscellaneous items as noncash awards and net gambling receipts. Prior to 1960

Table 3.—Adjusted Gross Income Gap, Total and by Type of Income, 1947-78

(Billions of dollars)

Year	BEA-derived AGI	AGI of IRS	AGI gap	Wages and salaries	Pensions and annuities	Farm proprietors' income	Nonfarm proprietors' income	Personal dividend income	Rental income of persons	Personal interest income
1947	172.7	148.7	23.0	4.3	0.3	10.6	1.9	1.4	2.7	1.8
1948	184.7	165.3	19.4	3.5	0.3	9.1	2.1	1.4	2.9	1.8
1949	184.0	166.0	18.0	3.5	0.3	7.8	3.0	1.4	2.4	2.1
1950	202.7	178.1	24.6	3.5	0.3	6.8	4.3	2.0	2.6	2.4
1951	222.8	202.3	20.5	4.0	0.4	7.3	4.0	1.8	2.0	2.7
1952	241.9	211.3	30.6	4.0	0.4	7.3	5.1	1.9	2.1	2.8
1953	254.7	228.7	26.0	4.4	0.5	6.8	5.0	2.1	2.2	3.4
1954	254.9	228.2	26.7	4.4	0.5	6.8	5.0	2.1	2.2	4.4
1955	273.0	248.7	24.3	4.7	0.5	4.1	5.8	1.9	3.1	5.1
1956	286.5	261.7	24.8	5.4	0.9	4.1	4.6	1.9	2.9	5.7
1957	302.1	280.3	21.8	6.8	1.0	4.3	4.1	1.9	3.1	6.7
1958	312.8	281.2	31.6	8.4	1.1	4.7	4.3	1.9	3.3	7.2
1959	326.2	302.1	24.1	6.9	1.4	4.4	4.3	2.0	3.0	7.6
1960	345.1	318.5	26.6	6.1	1.8	3.0	4.8	1.5	2.9	8.0
1961	360.4	320.8	39.6	6.6	1.8	4.0	5.3	1.4	2.8	7.6
1962	380.7	343.7	37.0	8.0	1.9	4.3	5.5	1.4	2.8	8.4
1963	400.8	368.0	32.8	8.9	2.0	4.0	5.0	1.4	3.0	8.9
1964	424.0	388.7	35.3	8.7	2.4	4.0	5.2	1.3	3.0	9.0
1965	457.3	428.2	29.1	7.0	2.7	4.5	5.2	1.3	3.1	11.1
1966	512.9	483.5	29.4	11.8	3.0	4.5	5.3	1.6	3.8	11.9
1967	545.2	504.0	41.2	9.0	3.5	3.9	5.9	2.1	3.7	12.3
1968	592.9	554.4	38.5	11.1	3.4	4.9	6.4	2.5	3.9	13.2
1969	652.7	604.5	48.2	8.8	4.0	6.3	7.8	2.3	4.2	14.8
1970	685.1	631.7	53.4	10.2	3.0	6.5	8.0	1.9	4.4	17.0
1971	730.5	673.9	56.6	10.2	2.9	6.6	8.4	2.5	4.3	17.2
1972	803.3	748.0	55.3	7.2	6.9	8.8	10.9	2.7	4.7	17.8
1973	901.4	827.1	74.3	10.5	7.2	14.5	11.8	2.9	6.7	21.8
1974	978.6	901.5	77.1	1.7	7.8	13.3	12.8	3.0	8.3	25.1
1975	1,019.6	947.8	71.8	5.2	6.6	9.7	14.9	2.7	8.8	28.9
1976	1,132.1	1,053.9	78.2	2.8	10.4	10.1	18.2	3.0	9.0	30.7
1977	1,280.7	1,188.5	92.2	2.6	10.8	8.4	20.4	3.0	7.7	31.1
1978	1,400.0	1,302.4	97.6	7.0	12.1	13.8	20.5	3.6	7.8	35.6

it also includes income of residents of Alaska and Hawaii.

The adjustment of personal income by the exclusion of line 2 and the inclusion of line 10 provides a measure that conforms to the IRS definition of AGI. The difference—the AGI gap—between BEA-derived AGI (line 16) and AGI reported by the IRS in *Statistics of Income* (line 18) is shown in line 17. The AGI gap can be taken as evidence of noncompliance with the tax code, but with the following caveats: the AGI gap includes (1) income earned by low-income individuals who are not required to file income tax returns, unreported income identified by IRS audit programs that is included in personal income, and gross errors and omissions in lines 3 through 9 and in lines 11 through 15 in table 1; and (2) the net effect of errors in AGI of IRS (line 18) and personal income (line 1). However, for two main reasons, an AGI gap cannot be taken as evidence of an understatement in GNP. First, data from the individual income tax returns are used only to a limited extent in the estimation of GNP. Second, where these data are used, BEA adjusts them for underreporting on the basis of IRS audit programs.

AGI by type of income

The adjustment of personal income to the IRS definition of AGI can be extended to the types of income included in personal income and in AGI of IRS (table 2). For example, the wages and salaries component of personal income is reconciled to wages and salaries in AGI by subtracting imputed wages, tax-exempt military pay and allowances, and adding the wages and salaries of residents of Alaska and Hawaii prior to statehood and the taxable portion of other labor income, such as fees received by directors and jurors. Dividends included in personal income are reconciled to dividends in AGI by subtracting dividends retained by fiduciaries, dividends received by nonprofit institutions, the dividend exclusion, and adding to it dividends received by residents of Alaska and Hawaii prior to statehood. Table 3 shows AGI derived from personal income, total and by type of income, for 1947-78, table 4 shows AGI of IRS, total and by type of income, for the same period, and table 5 shows difference between the two.

As a percent of BEA-derived AGI, the AGI gap declined from about 13 percent in 1947 to about 7 percent in

1978 (table 6). This decline reflects shifts in the distribution of BEA-derived AGI among income types with different percentage gaps and changes in the size of these gaps for individual income types. (Percentage gaps—that is, AGI gaps as a percentage of BEA-derived AGI—by type of income are shown in table 7.) The largest factor in the decline was farm proprietors' income. Its share in BEA-derived AGI declined over the period (from about 8 percent in 1947 to 1 percent in 1978) and it had a high percentage gap (about 74 percent in both years). Wages and salaries were also a major factor. The share increased (from about 69 percent in 1947 to 78 percent in 1978) and it had a low percentage gap (which declined from 3.5 percent in 1947 to 0.6 percent in 1978). Changes in several types of income worked in the opposite direction. The largest effect came from personal interest income. Its share in BEA-derived AGI increased (from about 2 percent to 7 percent) and it had a high percentage gap (which, however, declined from 48.6 percent in 1947 to 35.9 percent in 1978).

Some specific developments that affected the AGI gaps by type of income can be identified. These will be described below.

Wages and salaries gap.—Wages earned by U.S. citizens living abroad increased rapidly in the 1970's. These wages are part of the gap because the reconciliation does not take into account their exclusion from personal income and their inclusion in AGI of IRS.⁴

A persistent decline in the percentage gap is traceable to several develop-

4. U.S. citizens living abroad are required to file U.S. income tax returns even if all of their income was "earned income from personal services performed in a foreign country." Thus AGI includes income earned abroad; personal income excludes such income. However, no adjustment has been made for income earned abroad in deriving the AGI gap because data were not available when the 1980 revision of the national income and product accounts was undertaken. Recently, IRS has published *Statistics of Income—1972-1978, International Income and Taxes, Foreign Income and Taxes Reported on Individual Income Tax Returns*. This report shows that the total income earned abroad in excess of tax-exempt amounts increased from about \$0.5 billion in 1972 to \$4.8 billion in 1978. It also shows that wages and salaries were a significant portion—over 80 percent—of all foreign earned income in 1975.

ments. Rising income levels and minimum wage laws have reduced the relative importance of income earned below the withholding and filing requirements; even earners who would not otherwise need to file do so to secure refunds. The number of workers not covered by the withholding system has declined; consequently, a high percentage of wages and salaries is reported on tax returns. In addition, there is some evidence—although insufficient for making an adjustment—that some pensions and annuities are being reported as wages and salaries on tax returns. Such misreporting might have contributed to the narrowing of the wage gap.

Nonfarm proprietors' income gap.—Growth of the nonfarm proprietors' income gap may be due in part to corporate partners' shares in joint ventures. This item is included in personal income but not in AGI of IRS. However, no data exist with which to estimate the corporate partners' shares, and thus no adjustment can be made in the reconciliation. Understatement of nonfarm proprietors' income on tax returns also may be a factor. IRS audit programs have disclosed a growing understatement on the returns as filed. Because the results of these programs are taken into account in estimating personal income (and thus in BEA-derived AGI) but are not in AGI of IRS, such understatement contributes to the growth of the nonfarm proprietors' income gap.

Personal dividend income gap.—A sharp drop in the gap in 1954 coincided with the enactment of the dividend received credit and the dividend exclusion. Beginning 1954, individuals were allowed to exclude the first \$50 of dividends from their taxable income (\$100 for joint returns) and to subtract, as a credit from the tax, 4 percent of the dividends received in excess of the exclusion. The tax credit was reduced to 2 percent in 1964 and eliminated entirely in 1965; at the same time, the exclusion was increased to \$100 (\$200 for joint returns).

Personal interest income gap.—Several factors known to have affected the gap cannot be quantified. The gap includes the nontaxable portion of life

insurance annuity interest received by a surviving spouse, which should be removed from personal interest to obtain BEA-derived AGI. A surviving spouse may exclude up to \$1,000 of interest as-

sociated with annuities. When an annuity plan using life insurance proceeds is set up, the value of proceeds at the time of death is prorated over the an-

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Table 6.—Adjusted Gross Income Gap as a Percentage of BEA-derived AGI, by Type of Income, 1947-78

(Percent)								
Year	Total AGI gap	Wages and salaries	Pensions and annuities	Farm proprietors' income	Nonfarm proprietors' income	Personal dividend income	Rental income of persons	Personal interest income
1947	12.3	3.5	55.3	74.1	8.8	24.9	54.9	48.5
1948	12.4	4.2	48.9	83.8	9.1	23.3	52.7	47.2
1949	12.7	4.9	34.2	89.4	14.2	21.5	44.1	45.1
1950	11.6	3.8	41.0	84.2	17.6	24.4	43.9	47.8
1951	11.7	3.9	43.7	86.7	18.0	22.1	46.0	47.4
1952	11.0	3.3	42.7	84.8	19.5	24.7	47.1	49.9
1953	10.9	3.2	43.9	83.9	21.2	28.4	47.0	53.0
1954	10.1	1.3	39.9	59.0	18.3	31.2	49.3	52.1
1955	9.8	2.2	44.1	52.2	19.7	19.8	43.9	52.8
1956	8.4	2.7	48.8	61.8	15.1	8.7	44.9	54.4
1957	8.0	2.9	45.9	47.8	18.2	6.5	47.1	65.0
1958	10.1	3.5	45.0	51.9	19.7	7.9	49.4	64.4
1959	8.2	2.7	48.4	57.4	18.5	8.5	51.3	51.5
1960	8.4	3.0	49.3	60.6	17.3	11.7	45.6	50.8
1961	8.5	2.4	48.7	64.2	18.4	10.1	43.3	53.8
1962	8.4	2.7	44.5	51.6	15.9	11.4	41.8	52.8
1963	8.0	2.2	42.8	58.4	15.3	11.5	40.3	49.4
1964	8.6	2.6	43.1	60.5	16.1	15.5	51.1	47.6
1965	8.2	2.0	43.9	53.1	15.1	16.8	50.1	48.5
1966	8.7	3.0	40.1	56.3	15.7	11.5	49.8	48.9
1967	7.6	2.1	40.7	50.2	15.1	13.0	51.3	44.3
1968	7.6	2.4	36.2	55.6	13.2	14.3	51.2	43.1
1969	7.5	1.9	36.9	60.2	15.7	12.6	54.1	41.8
1970	7.0	1.8	38.9	65.5	17.3	10.9	55.5	43.6
1971	7.8	1.8	38.9	71.1	18.0	13.8	54.5	49.9
1972	7.4	1.2	38.4	63.7	19.0	14.0	57.0	38.3
1973	8.2	1.5	35.5	62.6	19.4	13.3	51.3	39.8
1974	7.5	1.2	32.0	71.0	22.0	12.5	52.1	37.8
1975	7.0	1.7	29.8	67.5	23.1	11.1	49.7	36.6
1976	8.0	1.3	29.8	68.4	24.7	10.7	43.9	33.7
1977	7.4	1.8	27.2	80.4	24.6	13.7	57.7	35.8
1978	7.4	1.8	28.6	74.6	23.3	10.1	56.0	35.8

Note.—Data were made in the *Statistics of Income* sample site after 1971. In 1971, about 0.26 percent of the individual income tax returns filed were included in the sample. By 1978, the percentage dropped to 0.18 percent. As a result, the variances on most income components increased and so did those of the annual swings in the AGI gap as a percentage of BEA-derived AGI.

Table 7.—Percent Distribution of Adjusted Gross Income Gap, by Type of Income, 1947-78

(Percent)								
Year	Total AGI gap	Wages and salaries	Pensions and annuities	Farm proprietors' income	Nonfarm proprietors' income	Personal dividend income	Rental income of persons	Personal interest income
1947	102.8	18.3	1.2	44.6	6.4	6.2	12.0	7.9
1948	100.0	22.8	1.2	39.1	8.9	6.1	12.6	8.3
1949	100.0	27.7	1.0	33.1	13.0	6.1	10.3	8.8
1950	100.0	23.2	1.8	37.9	18.0	6.4	10.0	10.5
1951	100.0	24.2	1.4	20.3	17.1	6.7	10.8	10.1
1952	100.0	22.6	1.6	27.1	19.1	7.2	11.7	10.6
1953	100.0	22.4	1.0	24.1	20.6	7.5	11.3	12.2
1954	100.0	28.0	2.1	20.3	19.4	5.2	12.6	17.3
1955	100.0	28.3	2.6	15.9	22.1	3.6	11.7	19.1
1956	100.0	30.3	3.2	15.9	10.7	2.9	10.3	20.6
1957	100.0	24.4	3.4	12.8	23.9	2.3	11.0	24.2
1958	100.0	26.8	3.4	14.8	19.9	2.4	10.8	22.6
1959	100.0	22.3	4.4	14.2	20.4	2.8	11.4	24.4
1960	100.0	24.3	4.8	15.3	17.3	3.9	9.0	24.5
1961	100.0	31.4	5.7	15.1	20.3	3.7	8.8	24.4
1962	100.0	25.0	5.8	13.3	17.3	4.3	9.3	24.2
1963	100.0	31.7	6.8	14.4	17.6	4.6	9.3	24.0
1964	100.0	32.2	5.8	13.0	16.0	4.9	9.4	25.7
1965	100.0	28.3	7.1	11.9	15.2	4.9	10.6	29.1
1966	100.0	28.2	8.7	13.3	15.4	4.1	7.0	28.5
1967	100.0	31.8	8.4	0.5	15.0	5.1	5.9	29.7
1968	100.0	24.5	7.5	10.8	14.0	5.6	8.5	29.1
1969	100.0	18.9	8.2	12.9	15.8	4.6	8.5	30.1
1970	100.0	18.8	9.3	11.9	15.8	3.6	8.1	32.7
1971	100.0	17.9	10.4	11.5	16.5	4.4	8.0	31.3
1972	100.0	12.2	11.6	14.4	17.8	4.6	9.5	23.0
1973	100.0	14.1	8.6	10.8	15.6	3.9	7.7	29.4
1974	100.0	2.3	10.7	21.0	12.0	4.1	8.7	34.3
1975	100.0	7.2	12.4	13.5	20.7	3.5	7.8	34.7
1976	100.0	9.0	13.3	15.0	23.3	7.7	8.3	32.9
1977	100.0	8.9	11.8	10.2	22.1	5.5	8.4	33.7
1978	100.0	6.8	12.7	11.4	19.5	5.6	7.6	34.3

affected by exchange market intervention activities by these authorities and by their investment decisions, particularly by OPEC members after the sharp increase in petroleum prices led to large accumulations of their investible funds.

By area, payments to Western Europe—mainly Germany and, to a lesser extent, the United Kingdom,

France, and Switzerland—accounted for about 50 to 60 percent of total Government payments in 1970-80. Payments to Japan increased rapidly and accounted for about 15 percent in 1980, compared with 8 percent in 1970. Payments to all these countries largely reflected their accumulation of dollars as a result of intervention purchases to

limit the appreciation of their currencies against the dollar. Payments to developing countries in Asia and Africa were 22 percent of all Government payments in 1980, compared with 7 percent; they were largely to OPEC members. The share of total payments to other countries and international organizations declined.

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nuity period for the purpose of computing the interest element of the annuity, and the amount determined by such proration is nontaxable. However, the amount of an annuity installment that exceeds this prorated portion is the interest element that is taxable and included in AGI of IRS.

Interest income received by minors from savings accounts and from U.S. savings bonds in their name is included in BEA-derived AGI. A minor, like an adult, is taxable for his wages and for the income received from nonwage sources. However, when the total income of a minor is less than the minimum re-

quiring a tax return, it is likely that such income is not reported to the IRS, especially when taxes are not withheld from the wage sources. Also, if a minor is under 19 or a student and qualifies as a dependent of his parents, a tax return is required only when unearned income exceeds \$1,000. (Interest received by a minor is most likely to be reported when he received wages subject to withholding and files a tax return to secure a refund.) Interest received by minors could be substantial and it is probably the nonwage income source from which minors not required to file most often derive income.

When U.S. savings bonds are purchased in a minor's name by the parent, the availability of the option of reporting the interest earnings on the accrual accounting method makes it unlikely that the interest earned will be reported to the IRS unless the minor's total amount of taxable interest accruing each year exceeds the minimum requiring a tax return.

Interest earned on individual retirement accounts (IRA's) is included in BEA-derived AGI, but not included as interest in AGI of IRS. Instead, such earnings are reported as pensions and annuities in the year the funds are withdrawn.